CURRENT SITUATION, FUTURE TRENDS OF FREE ECONOMIC ZONES AT THE THESHOLD OF THE GLOBALIZATION ERA

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The term of globalization is used both in descriptive and normative senses. It describes a process of integration and growing interdependencies where national boundaries become less and less important in decisions to be taken by economic agents. The normative perspective assumes that the full liberalization of market forces through open trade and foreign investment regimes will stimulate sustained growth and greater convergence of income per capita throughout the world. Trade and Foreign Direct Investment (FDI) have witnessed strengthening of regionalism, and there has been a "partial globalization" for other capital flows. Free flow of goods, capital, labor, technology, information has provided great developing opportunities, the speed and scale have not allowed enough time and capacity for the developing countries to prepare proper institutional settings in their own pace.

On that note my essay is about the background, development, current status, future trends of free economic zones, incentives offered by international practices to attract investment, their strenghts and weaknesses, experiences and lessons learned by the countries that established free zones, particularly the specifity of free economic zones in China, its impact on the country's economy as well as incentives offered by Chinese Government to foreign investors.

Over the last 2-3 decades, the countries started to establish free economic and trade zones in order to foster economic development of selected areas.

The first free zone was initiated in Gdansk by the end of last century conditioned by tax and customs duty exemption. Laws on customs free zones at were passed in the USA and other countries during 30s and 40s of last century. Free industrial export zone was established in Shannon Airport of Ireland at the end of 1950s and international law on free zone was adopted during 1970s and 1980s. In this way, free economic zones were established all over the world and thus became one of the important factors that accelerate country's economic growth and development.

According to UNCTAD , there are currently about 900 free economic zones operating in over 80 countries, from which 40 zones in Middle Asia, 50 zones in

Latin America, 80 zones in Europe, 110 zones in Mexico, 124 zones in China, 213 in USA and 225 in Asia respectively.

Although developing countries commonly use this method to attract investment and improve infrastructure in their distinct regions, however, developed countries also use such zones to promote regions lagging behind in terms of development. Over the last decade, there were free zone boom occured in North-East Asia. Recently, free economic zones are being established in large numbers in the countries with transition economies. (www.FEZ.com).

In addition, China had reached agreement with Russia and North Korea to establishment an international free economic zone at the beginning of 1990s based on the enormous natural resources available in the bordering region around Tumen River basin. While UN is making concerted efforts to support this initiative of three countries, no one except China is pursuing the case. The UN has developed large and long-term project on "Development Programme of Tumen River Region" and, according to the initial estimates, US$ 30 billion would be needed to implement the project. It will initially cover two regions namely "Tumen River Economic Zone"(Hunchin-Posiet-Rajin) and "Tumen River Economic Development Zone"(Tianjin-Vladivostok-Chonjin). However, there is no significant progress to date due to the current situation on the Korean Peninsula and to many other reasons.

The countries that intend to establish free economic zones to attract foreign investment use wide range of incentives. The next section will briefly discuss these incentives.

Incentives for Foreign Investment

At present, many countries are actively pursuing ways to attract foreign investment. In this connection, there is steeply decreasing tendency to prohibit, restrict and limit foreign investment around the world. Foreign investment is not only an act of transfering physical and non-physical capital from one country to another, but it also benefits the receipent country as much as investment it receives since foreign investment had numerous economic advantages.

Many countries in the world widely use incentives to attract investment. Incentives play an important role in creating favorable environment to ease barriers and obstacles to investment by means of tax exemption, reduction in tax, rates, provision of financial support and infrastructure development. Therefore, the extent of increase in foreign investment depends on how precise the incentives are. Nevertheless, it may cause damage to country's economy if its economic importance is over-emphasized.. So, it is critical to know what is an incentive, in what forms it can be and what are their roles.

While this brief information is designed to answer the above-mentioned questions, we wish that you would recognize it as our genuine intention to make contribution to Mongolia's effort to attract and promote foreign investment.

As defined in the book "Incentives and Foreign Direct Investment" published by UN in 1996, the incentive is provision of superior economic right in certain degree by Government to the special companies in order to promote and support their proper operations. In other words, the investment incentive is also defined as financial support or advantage offered by either Government or other institutions to individuals or legal entities. According to the research study on Investment Incentives and Disincentives and the International Investment Process" carried out by the OECD (Organization for Economic Cooperation and Development), the investment incentive is defined as the government measure that might impact on investment decisions, or possibly increase profit from potential investment, and/or reduction of investment risks. Distinct character of the investment incentive is its independence from market size, comparative advantage that affect investment content and atmoshpere, price fluctuation and socio-economic factors. The investment incentive is derived from the difference between social rate of return and private rate of return, and is the foreign investment policy tool to eliminate this difference.

As foreign investment is not only capital flow, it is always accompanied by and facilitates transfer of non-material resources such as advanced technology, management skills, know-how and multinational network If investor can increase level of return by exploiting non-material capital, then there is no need to apply incentives. Let us this: In terms of foreign investment, investors invest capital with the objective to increase the rate of return by fully exploiting available resources. However, the recepient country does not often provide favorable conditions for investors to make profit. From the point of view of recepient country, foreign investment is always an important channel that leads to economic growth, employment generation, industrial capital formation and transfer of newly advanced technology. Although the recepient country is often interested in generating economic growth through foreign investment, it does not commonly satisfy the demand of investors. Countries make efforts to apply decisive action towards resolving weaknesses by using internal resources. The ways and means by which countries are trying to create more favorable business and investment environment by their own resources and efforts are considered as investment incentives. Other two incentives can be mentioned excepted one derived from the differences between social and private return ratio of return and private rate of return of investment. Firstly, incentives can be offered to compensate the return loss in case of profit loss caused by the government intervention.

Secondly, if investors bear significant amount of expences beyond expected due to underdeveloped infrastructure and deficiency of service sector of the recepient country, the incentives can be provided to investors as an to compensation of extra expenses.

Finally, it is apparently difficult for the countries interested in attracting foreign investment to get rid of its obstacles to investment in short-term. Therefore, they often offer incentives to resolve the above-mentioned problems along with attracting more capital. In addition, this is a tool, content of which can be easily changed and coordinated compared with other factors affecting decision about investment.

Types of Foreign Investment Incentives

There are several types of investment incentives. Foreign investment incentives were given great importance, particularly by the end of 1980s. Thus, incentives became competing tools with each other and the types of incentives have increased in numbers. Furthermore, government organizations from same country offered varied incentives. Incentives vary in its objectives.

There are three types of incentives such as fiscal incentives, financial incentives and other incentives. Other incentives include types of those except includes in both fiscal and financial. Developed and developing countries widely apply fiscal incentive measure, whereas financial incentives/ monetary aid are offered in developed countries. For least developed or developing countries, it is rather difficult to encourage investment through financial incentives than fiscal. Mongolia is also in the same situation as others.

Tax Incentive

Tax Incentive is the most widely used incentive among three types available. According to the first half of 1990s the research conducted by UN in 103 countries, there are only 4 countries that do not offer tax incentive to investors. The usage of tax incentives had increased in 1990 compared to the middle of 1980. However, there was no change in its content. The main example of tax incentive is decrease in the rate of tax. In other words, the standard rate of tax is decreased for all foreign investors. Despite decrease in the rate of corporate tax, tax exemption is also used. It is called tax holiday and in most countries, tax exemption incentive is offered to foreign investors for the first 5 years since commencement. In some countries, foreign investors can enjoy tax exemption incentives for about 10 to 25 years. Tax exemption incentives can be offered to investors during tax holiday period when investment had not yet brought returns whereas taxes could be charged if investment started to bring its returns. If an investor could not make profit during tax exemption period, there is a possibility to provide further tax exemption depending on future profitability of investment.

Apart from the above-mentioned incentives there could be incentives such as reduction in tax rates or cuts in the amount of payable taxes. For instance, it allows depreciation, fast depreciation and instant depreciation of industrial equipment. This is a form tax concession to foreign investment entities allowing to deduct these deprecition from taxable income. There is another incentive that offers deduction in taxes for the amount that equals to certain percentage of the invested capital. How it successfully, the companies can enjoy tax reductions. For example, reduction in taxes can be offered to the companies if certain percentage of its income accounts from local content. Another non-tax incentive is exemption from social security contributions.

There is by export and import taxation system for foreign invested companies. For instance, incentive of tax exemptions are provided to foreign invested companies when it import equipment, spare parts and raw materials to operate. Exemption from customs duty are usually offered for 5-10 years in the most of foreign countries. Sometimes it can be for 15-25 years. Incentive to reduce and exempt from export and import taxes are mainly used in Foreign Investment District and Foreign Investment Zone.

The most of commonly used tax incentive related to exports is export tax exemption for foreign invested companies. Besides, it can also offer reduction in tax by certain amount or reduction in the amount payable. Fierce competion among the countries for offering various tax incentives to attract more foreign investment could result in threat of harmful tax competition. Extremely low tax rates to attract investment in one country against neighbors not only result in conflict between them but it may also cause difficulties in the country's financial situation. According to the research by the OECD, harmful tax competition tends to spread in the era of globalization, and hence, there is a need to take legal measures in international level against such threat of harmful tax competition. In the process of drafting foreign investment law, South Korea sets 10 years for tax reduction that is consistent with the countries such as Malaysia which always activily competes to attract investment. Please refer the following table for the main types of tax incentives.

Table. Main Types of Tax Incentives

Income related	Exemption of tax Harmonized with future profit if company incurs a loss within the period of tax exemption
Capital related	To allow fast deterioration Reduction of tax for investment and reinvestment
Working force related	Exemption of social security rate Reduction of taxes based on number of newly generated job opportunity
Value added	Reduction of taxes based on the percentage of industrial input from domestic market reduction of taxes in the process of value added
Import related	Exemption of import tax of equipment, raw material, spare parts Exemption of customs tax Reduction of import customs tax
Export related	Exemption of export customs tax Reduction of tax on income generated from export Reduction of taxes on foreign currency income Reduction of taxes based on comparition between export and domestic sales Repayment of customs tax Reduction of taxes based upon percentage of industrial input from domestic market Exemption of corporate tax based upon the calculation on expenses of export industry and expenses abroad
Other specific costs related	Reduction of corporate tax based upon costs of marketing, other additional operational costs

Source: *UNCTAD (1996) Incentives and Foreign Direct Investment (New York- United Nations), p.4.*

Financial Incentives

Financial incentive is the direct financial support or aid other than the reduction or exemption in taxes for foreign investment companies offered by the Government of recepient country. As stated in UN research, 59 countries from total of 83 countries have granted financial incentives in the early 1990s. Developed countries widely apply this type of incentives and it is generally used as a tool for implementation of policies regarding regional development, study, research and SME promotion.

The main key of financial incentive is a monetary support either to physical component of investment project or to access for provide additional costs. In the USA and England, the financial incentives are offered to foreign invested companies by central or local institutions.

Financial incentives can be offered based on the number of job opportunities created by the company. If foreign invested enterprises do not meet terms and conditions, monetary aid/ financial incentive can be recalled.

Various types of financial incentives are offered except cash support. Particularly, granting the loan with low interest rate etc. Sometimes, the governments of the recepient countries issue bank guarantee for loans to foreign invested companies. There is another practice to issue a governmental guarantee on Letter of Credit to foreign invested companies by financial institutions of the recepeint country. In case the company invests in risky business, the government and financial institutions of the country together will apply incentives such as joint investment or engage in state insurance programs to prevent from risks of currency fluctuations and inflation.

According to comparative study between tax and financial incentives, we can see the difference as follows:

Firstly, while tax incentive is generally applied to all sectors of economy, whereas financial incentives are offered based upon policies concerning regional development, improvement of research work and promotion of SMEs.

Secondly, tax incentive directly involves participation and responsibility of tax authorities, whereas financial incentive is policy-driven. The major types of financial incentives vary as follows:

Major Forms of Financial Incentives

Government aid	Direct monetary aid related to investment project Monetary aid for production and distribution costs
Government soft loan	Loan in the form of monetary aid Guarantee on repayment Guarantee on letter of credit
Government involvement	Jointly invest in sector in risk
Government insurance Scheme	Government insurance to prevent from foreign currency fluctuation, inflation and other threats not directly related to production

Source: *UNCTAD (1996| Incentives and Foreign Direct investment (New York United Nations), p.6.*

Other Incentives

This kind of incentive is called as both market advantage incentive and service incentive. Incentives in this category are not included in tax or financial incentive groups. It proves that foreign invested enterprises are open to receive supports from governments in many different ways. Measures to improve country's infrastructure and provision of information to foreign invested enterprises are included in this type of incentive.

As mentioned above, such service incentive related to infrastructure improvement is widely offered in Exporting Processing Zone of South Korea, and other zones with advanced industrial technology. Types of other incentive are listed below:

- Matching foreign invested enterprises with domestic counterpart;
- Advisory services on implementation of investment project;
- Market Research;
- Provision of important information;
- Assisting in establishing contacts with raw-material supplier;
- Support production and marketing process;
- Provision of training.

On the other hand, governments sometimes offer incentives to foreign invested enterprises to have monopoly in a sector or to restrict rights of other enterprises to operate in this sector. This types of incentives are widely used in under developed countries. There are also rarely used service incentives such as temporary provision of foreign currency. The following is the potential types of other incentives:

Other Incentives

Infrastructure improvement	To establish infrastructure
Service provision	- Matching foreign invested enterprises with domestic counterpart; - Advisory services on implementation of investment project; - Market Research; - Provision of important information; - Assisting in establishing contacts with raw-material supplier; - Support production and marketing process; - Provision of training
Provision of market advantage	To issue monopoly right To issue right to operate solely in that sector
Superior right of foreign currency service	Government supply of foreign currency Special permit for remittance of profit and capital

Source: *UNCTAD (1996) Incentives and Foreign Direct investment (New York United Nations), p 6*

Benefits of Investment Incentives

We considered investment incentives that are recognized as the most beneficial and wide-spread tool among other measures in today's international practice. Most of the countries widely use the above-mentioned 3 types of investment incentives to encourage investment inflow. Let us discuss effects of incentives. As stated in the research by OECD, the investment incentives in very limited extent influence investors' decisions on investment and selection of investment forms. Additionally, market prospects and costs are included as the main factors that significantly influence decisions to make investments. To research carried out by the UN reveals that incentives can not play important role in selecting an invesment destination for foreign investors, particularly for multinational corporations. In fact, the main factors influencing on decision-making to select investment destination for multinational corporations are not investment incentives but market size of the country, economic growth tendency, production costs, technology level, infrastructure, political stability and level of control. Investment decision making process includes decision making process as well as overall size of investment. Investments can be made in forms of joint venture with either majority equity position or minority equity position, Greenfield investment, M&A. Mergers and Acquisition etc.

It is evident that incentives influence little when investors make investment decision, but they effect to certain extent to the final decision of investors after the selection of destination. Let us make explanation to this. Let us assume that on investor needs to make investment in Asia and targeted at several Asian countries. Provided that these countries are similiar to each other in terms of their economy and market conditions, and hence, the incentive will be the final criteria of which countries will be selected as an investment destination. Sometimes, incentives influence in the selection of area where investment to be made within a given country.

As incentives help to decrease costs of investment process, it promotes investments into stabilized markets rather than growing one. However, foreign invested companies that attached great importance to incentives could no longer maintain its operation compared to those who paid attention to other factors as they always have interest in receiving incentives.

Investment incentive does not produce an effect on timing of investments. For instance, sometimes, incentives can be slowed down due to slowing phase of financial accounting and repayment. In this case, investors may lose golden moments of investment. Therefore, it reveals that other factors such as market, agreement reached between investor and government will substantially influence on investment decsion making rather than investment incentive alone. Furthermore, owing to different strategies among investors, incentives can vary in the degree of importance. Investors who invest in export industry using cheaper labor force prefer tax incentive rather than service incentives. Therefore, it implies that wider application of tax incentives are likely to have more influence on export-oriented investment.

Countries create incentives with pursuit of objectives to promote export, increase employment, introduce advanced technology and create value added. Among those objectives, the incentive to promote export is believed as the most productive one. It is worth noting that if objective of incentive is underestimated and vague, its importance would decrease, even it may cause no return. Although countries define their investment incentives considering both foreign investors strategy and objectives of the economy and investment of the country, it is common for neighboring countries to offer similiar investment incentives. If this phenomena further continues, it will result in adverse effect on international trade and proper distribution of resources. In this case, incentive policy is coordinated by decreasing number of less important incentives rather than decrease in nominal size of incentives. The next section will discuss free economic zone and its types.

Free Economic Zone, Types, Strengths and Weaknesses, Experiences and Lessons Learned

Types of Free Economic Zone

Free economic zone is divided into certain categories. No matter of developed or developing status, the countries establish free economic zones as tools to improve infrastructure and promote foreign investment. The selection of the most suitable type of free zone for selected area depends on many factors. Those factors include location, current status and future prospects of infrastructure, level of industrial development, services, legal system. Free economic zones are classified into the types (specific districts, countries) as listed below:

Free port – free trade zones (Hongkong, Singapore)

This type of zone is distinct by its establishment in small developed countries, surrounded by big markets, where import and export taxes are rather low or absent, and well developed service sector. This sector is capable to promote and facilitate international business flow by providing powerful services such as logistics, banking, and insurance etc.

Free Economic Zone (Shenzhen, Batam)

As this zone has been established in big countries like China and Indonesia, the preferential taxes and other factors are recognized as impetus to foster economic development. Also, professional services play an important role in running production.

Free Export Zone (South Korea,Taiwan, ASEAN)

The features of this zone is its location with well-educated professional workers and tax exemption on import of necessary inputs for export production. Therefore, domestic sales were strictly controlled for FEZ firms to protect local entrepreneurs from the competition, and the government paid intensive attention on this dynamic effects. The effect were measured as 1) technology transfer and industrial linkage between FEZ and local firms, 2) human capital development , 3) demonstration effects etc.

Free Export Zone (Panama, Abu Dhabi)

All goods necessary for re-export are exempted from taxes in this zone, which is located in the main road junction and near the central market.

Free Export Zone (USA)

In order to process all materials to be used in future production into final products, all materials are exempted from taxation. This type of zone was established in the several states of USA with main markets and including vast area. In this zone, rights are offered to import large amount of goods, to enjoy discount on transportation fee and to postpone customs tax until all goods to be retailed out.

The following are the prerequisities:

- Transperancy Government Policy concerning free economic zone;
- Infrastructure established by Government;
- Mature logistics and customs service system;
- Professional/ non professional working force paid on the basis of competition;
- Banking and insurance services;
- Good housing for migrant workers,comfortable environment, safety, and other conditions
- Economic and political stability;
- Mature legal system.

If there is a lack of one or more of the prerequesities, the operations of free economic zone can not be adequate. For instance, due to underdeveloped infrastructure in Batam Iseland of Indonesia, political instability in Sri-lanka, lack of working force in Malaysia, unmature service sector, the free economic zones in those areas failed to operate properly.

The objectives of free economic zones vary among countries and within the country. The common objectives are as follows:

- To enhance regional economic development;
- To promote foreign investment;
- To improve productivity by introducing new advanced technology;
- To improve infrastructure, to improve professional skill of working force;
- To experiment new economic system.

Let us touch brief about successful free economic zone examples of Taiwan and South Korea. Taiwan is one of the pioneering countries that established successful free export zones. These zones are mainly used as tools to establish new industries, to generate employment opportunities, to gain from exchange except export and to succeed in fulfilling their objectives. First 3 free export zones were established in Takao in 1966, Nanko and Daichu in 1971 respectively. Those zones covered area of 174 hectares with 70 thousand working people.

Taiwan sets several objectives namely to promote and support domestic and foreign investment, to develop export-oriented industries, to generate employment opportunities and to introduce advanced new technologies in order to establish these zones. In order to attract companies in these zones Taiwan offered incentives for certain companies such as exemption from customs tax, corporate tax and comsumer tax. As a result, total 270 industries launched operations in these zones, including electronics, plastics and car industries. In the beginning of the experimental period, exports generated in the zones accounted for the major part of export income of Taiwan. Export volume of the zones reached in US$ 2.3 billion that accounted for 70 % of the Taiwan's overall export income from 1967 to 1980s.

The economic development of Singapore, the center of South-East Asia, was facilitated by the foreign investment. Singapore has succeeded in becoming free economic zone for a short time by undertaking measures to set lower tax rates, to improve production, trade, logistics and banking services. Infrastructure was improved and service costs were set lower in Singapore. Since 1985, Singapore has been making great efforts to promote high value added industries through depth processing as well as to support trade, financial and other types of services. These resulted in large amount of foreign investment due to beneficial location of the city as well. Exception to the above mentioned countries, Hongkong, South Korea, Thailand and Malaysia are also succesfully operating free economic zones based on their specificity.

Free Zones of Russian Federation

In 1990, the proposal of establishing total 11 free zones was defined. Since then, Russia has been adhered to undertake this action. Among 11 zones, 4 in Far East namely in Chita, Sahalin, Primor and autonomic region of Hebrew. The Governors' Office of Primor region has paying great importance to active operation of free zone "Great Vladivostok free economic zone" (include the district of Nahodka city). This free economic region is located in the southern part of Primor and covers vast area bordering with port “Vostochnii” in the north and reaching “Hasan” lake in the south bordering with China and North Korea. Under the framework of UNDP assistance, Japanese Technical Consulting companies carried out the research studies in the beginning of 90s. The objective of Great Vladivostok free economic zone is to trade with Asia countries and to attract investment from them. Great Vladivostok free economic zone will run both import and export operations, based on the free port and multiple services available. This zone includes 3 sub-zones consists of the following cities: 1. Vladivostok city-central point with education, academic research and services; 2. Nahodka city specialized in intensive production with vast area; 3. Hesan city. Although there is no transportaion network and important infrastructure provided in this city, agriculture, fishing and food industry can be jointly carried out in conjunction with neighboring countries of China and North Korea. Development of Great Vladivostok free economic zone is implemented in 3 phases. First phase: based upon the current stock of internal resources, to run production , to sell products abroad and to import necessary facilities to improve infrastructure; second phase: to produce export-oriented products, to alliviate import dependency, to improve the product quality and bring it to the level of international standard; and third phase: to fulfill the objective to improve production technology of both domestic and export products to advanced level.

Due to the existing problem of inconcrete investment incentives, internal and external factors, these zones operate insufficiently and are still in the beginning phase compared to those in the neighboring China.

Free Zones of the People’s Republic of China

In 1979, as China allowed 2 provinces Guangdong and Fujian to apply flexible policy regarding economic foreign relations and cooperation, the free economic zones were established in these provinces. Another 4 free economic zones were established based in 2 provinces namely Shenzhen, Zhuhai and Shantou, Xiamen.

Shenzhen Free Economic Zone of PRC

This zone is considered as one of the most successful free economic zones due to the fact that this zone did not apply restrictions on investment sectors, development of real estate, trade, tourism (including casino). This zone was established to undertake experiments on implementation of principles of market economy that was allowed in China, and further disseminate results of the experiments to other provinces and districts. It succeeded in fulfilling these tasks and objectives.

The Shenzhen zone was established in 1980 with 27.5 square kilometers, attracted overall 569 investment projects worth of US$ 512 million for 10 years until 1990 and created 476 thousand employments opportunities. Export products worth of US$ 5 billion have been produced in 1990.

Shenzhen fulfilled its objective to serve as a platform whereby Chinese in overseas can contribute to the country's economic development.

Shenzhen ranks in the first place for its area of 27.5 square kilometers, while others are smaller namely Zhuhai-6,7, Shantou-1,67,Xiamen- 2,5, square kilometers. From this statistics, we can see that free economic zones account for 16% of total area of Guangdong province, a small part of total area of Fujian. Areas of these free zones were widened in 1983-1985, to 15.16 square kilometers in Zhuhai, to 52 sq.km in Shantou and to 131 sq.km in Xiamen.

China avoided the involvement in internal affairs of these zones and adheres to the principle to maintain their self-regulating administration. While adminisrative body of the zones was appointed by the central government in the early years, it is now under local government responsibility. In the first 5 years, the central government set a minimum amount of fund to invest to develop the zone that is supposed to be generated from the investors, and granted loans for industries that produce equipment, and exempted taxes. Chinese Government has been offering the following incentives to investors:

- Corporate tax is set at 15% for joint ventures provided if the joint venture has earned the amount equals to amount of investment, whereas corporate tax is 33% for joint ventures operating outside of the free zones and 55% for state enterprises.

➢ Granted soft loans at very preferential interest rate, subsidized very important enterprises and allowed fast depreciation, provided preferential reductions for investment and re-investment;

➢ In order to invest in vast construction work of free zones, granted permission to launch construction work worth of 50 million yuans for heavy industries, 30 million yuans for light industry without permission from the Central government.

➢ Offered incentives able to attract investors in terms of elecricity, water supply and land rent;

- In terms of land rent, set different rates for rent based on the features and importance of buildings;
- Exempted from land rent if the building is equipped with equipment and technologies to produce popular brands of multinational companies or advanced new technologies, and spare parts.
- Granted enterprises with rights to sell its products, to contact directly to partners, to set minimum wage rate, staff recruitment and discharge;
- Granted opportunities to invite and consult skillful experts from abroad;
- Allowed free remittance of profit after corporate tax;
- Reduction and exemption of customs taxes and preferential rates of customs taxes for imports on necessary products into the free economic zone and exports of products.

The aforementioned incentives substantially contributed to the development of export-oriented industries, trade and tourism. In addition, the zone succeeded in generating and mobilizing substantial amount of capital in very short time offering the investors with the range of investment opportunities. It is evident that brand new economic structure that is different from the traditional Chinese economic structure – centrally planned economy has been shaped. Two systems have been operating simultantiously within one country.

New management, administration and operational skills for enterprises, western management and policy of floating rate applied in the free economic zones significantly contributed to the process of economic reforms in China.

According to the experiences and lessons learned concerning free economic zone, China started to take actions to develop these zones in the forms of specialization and diversification. For instance, The Shenzhen free economic zone is distinct for its complex development features of tourism, international trade, high technological processing industries and human resource development. The Zhuhai specializes in food industry, tourism and trade. The Shantou mainly specializes in food industry. The Xiamen specializes in tourism, assembling of high tech products and electronics.

Since 1985 the policy towards free economic zones gradually changed towards promoting and developing export-oriented production. For example, industries became obligated to export 60% of its products. If the industry exported 70% of products, 10% of corporate tax could be levied. If more than 70% of products has been exported, the corporate tax could be even less, or could be exempted. Large amount of soft loans in terms of yuans or US dollars have been granted to the export-oriented industries.

The second phase of the development of free economic zone has started since 1988. Hence, renewed strategies were adhered to establish free economic zones and cities, China expanded the area of zones, joining small cities, districts near the sea and focused on know-how transfer, transfer new advanced technology and equipment from highly industrialized countries on credit. In this regard, it altered the export-oriented ownership zone strategy.

Free economic zone and ownership zone vary in their administrative status, features of administration and management. Ownership zones do not possess any administrative area. Local governments of cities near the sea directly administer those ownership zones.

Open cities with free economic zone status have been widely opened through borders and districts near the borders since 1990.

In 1992, it announced the following cities as open cities: Heihe and Suifeihe, Heilongjiang province/North-Eastern border/; Changchun, Jilin; Manzhouli, Inner Mongolia. In this regard, 4 big zones of "cooperation near border" have been established.

➢ Zabaikalsk-Manzhouli zone, based on the cooperation between Chita – Inner Mongolia province.

➢ Blagoveshensk-Heihe, based on the cooperation between Amur-Heilongjiang

➢ Pogranichni-Suifenhe, based on the cooperation between Primor-Heilongjiang province

➢ Craskino-Hunchun, based on the cooperation between Primor-Heilongjiang

In that year, the area of 40000 sq.km of 9 districts bordered with Russia have been opened. Few years ago, Erlian city bordered with Mongolia has been announced as open city, thus set objective to become free port city.

By the end of 1990, special attention was paid to establish free economic and technical development zone or information technology park in order to master new advanced technologies and equipment.

Since 2000, China has successfully applied models of free economic zones, open city, ownership zones in the implementation of its strategic plan to develop the western China.

As a resulf of concrete combination of forms of open cities, free economic zones and accumulation of experiences and lessons over the period, China succeeded in attracting the large amount of foreign investment into the country, and reached in today's plateau of high rate of economic growth and development.

While Chinese strategy to attract foreign investment has undoubtedly presented a great opportunity, it is worth to mention that it has resulted in some adverse effects and difficulties. Therefore, there might be insights and points to take into consideration for small countries like Mongolia.

The adverse effects

First: Due to loose control in free economic zones, ownership zones, and open cities, it resulted in steep increase in crime, people and business entities that enjoy superior rights of tax incentives. Researchers call it as " bucket without bottom".

Second: Due to the supportive measures concerning land use, some adverse effects have been caused in terms of ecological aspects. Therefore, the government stopped granting lands, except for establishment of high-tech park.

Third: Due to wide spread reduction in taxes, it caused less budget income. All enterprises with varying ownership are subject to universal 33% of corporate tax after changing different tax rates based on regional rating and other factors.

Fourth: Intention to establish "micro zone" at any expense was widely spread. In 90s, there were 8700 micro zones operated, and enjoyed rights more than free economic zones. Researchers called this "Free Zone Fever". Operation of 1000 zones have been suspended on the basis of insufficient fund to improve infrastructure, lack of permission, inefficiency, conflict and land use without any permission. China adheres to the view for not establishing other free economic zones in North-East, South –Eastern Region.

Conclusion

According to the experiences and lessons learned by the countries that succesfully established free economic zones, they have paid attention to the distinct and strategically important regions and issued those regions with free economic zone status to promote domestic and international investments, to develop export-oriented industries, to generate employment opportunities, to transfer advanced new technologies, and to expand economic foreign relations. In order to attract foreign investors the countries implement policies of flexible incentives, alter tax incentives such as reduction of taxes, customs taxes, as well as consumption tax. As a result, the factories have been established for short time, those produce only one kind of spare part of products produced by multinational companies specialized in electronics, micro parts and assembling high-tech products.

The countries often make efforts to improve its infrastructure and set low level service charges. Additionally, in the process of applying incentives, the countries pay attention to improve creativity and innovation and promote value added services, production, trade, financial and other services.

Resently the Government of Mongolia initiated Law of the Free zone, Law of the Status of the "Altanbulag" Free trade zone and Law of the Status of the Free Economic zone "Zamiin Uud" . These laws were adopted by the Parliament. The two zones are main gateways of import and export flow of Mongolia. The "Altanbulag" Free trade zone is located on the Mongolia-Russian auto road border and the "Zamiin Uud' Free economic zone is located on the Mongolia -Chinese railway border.

The "Altanbulag" Free trade zone establishment has begun, particularly feasibility study and land planning has already been done and infrastructure construction and administrative buildings will be completed in the current year. The Development of documents such as Industrial park development concept, Industrial development policies in rural area are under consideration by the government.

The upcoming international open bidding announced by Government of Mongolia to select a strategic investor to undertake the implementation and development of "Zamyn-Uud" Free Economic Zone (FEZ) that will consist of 3 main sections including tourism-services (including casino), trade and industry under the management agreement.

The "Zamiin Uud" Free Economic Zone Land area is located in the Mongolian border area and has 900 -hectare lands. Zamiin Uud border town is located in the Southern Mongolia 780 km from Ulaanbaatar, the capital city of Mongolia 240 km from Sainshand city, center of Dornogovi Province 4.5 km from the border of Mongolia and 8 km. from the Chinese border town "Erlian". Zamiin Uud is most biggest border complex of Mongolia.

The population of Zamiin Uud is 6.6 thousand but the daily every passenger flow is estimated it 2.5 thousand of both foreigners and Mongolian citizens. There are several facilities designated for border, customs and public service activities. For example, bulk transshipment facilities, railway transshipment facilities, border inspection facility with the capacity to pass daily 2000 passengers and 3000 cars, 13 hotels with 500 beds and 38 canteens and shake bars etc.

In terms of electricity supply, the Zamiin Uud is connected to the 110kV high voltage power line. Zamiin Uud has high-level communication possibility because it is connected to high-speed fiber communication line The line has gateway to international communication network. Thus, data and voice exchange, E-mail as well as Internet access, are available. There is also installed VSAT station.

Zamin Uud, as an administrative unit, belongs to 'Dornogovi province'.

It will establish free economic zone that offers favorable conditions for Silk Road and investment, having great international importance not only for Mongolia and its 2 immediate neighbors - strategic partners, but also for overall economic development of North-East Asia

International importance of the Zamyn-Uud FEZ is that it provides a favourable opportunity to create trade, investment and tourism network between South East-Asia and the Pacific and Europe. As a result, Mongolia will have a chance to take part in international flow of information, capital, foreign exchange, finance, goods, technology and tourism.

In my opinion the establishment of the FEZ will be a powerful driving force for the acceleration of Mongolia's economic growth and development that would increase growth of foreign trade four times and expand tourism three times. Therefore, it will provide a great opportunity to accelarate GDP growth four times and provide 100% employment for well-educated young labor force.

As a result of all these, Mongolian economy will be closer to the level of other economies in the region and will present historical opportunity to participate in the integration of North-East Asian economy. Therefore, we believe that Mongolia could hold certain shares in the North-East Asian trade pie, and hence, will have an opportunity to join the regional free trade agreement.

I believe that the "Zamiin Uud" FEZ has the potential to be the North East Asian version of Las Vegas.